VALLEY MENTAL HEALTH

Consolidated Financial Statements and Single Audit Reports

As of December 31, 2006 and 2005 and for the years then ended

(Together with Independent Auditors' Reports)

Index

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Valley Mental Health, Incorporated
Salt Lake City, Utah

We have audited the accompanying consolidated statements of financial position of **Valley Mental Health, Incorporated and Affiliates** (the Organization), as of December 31, 2006 and 2005, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of **Valley Mental Health, Incorporated and Affiliates** as of December 31, 2006 and 2005, and the changes in their net assets, and their cash flows, for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the consolidated financial statements, in 2006 the Organization changed its method of accounting for its investment in tax credit housing projects to adopt Emerging Issues Task Force Issue No. 04-5 - *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights.* Accordingly, such tax credit housing projects have been consolidated for financial reporting purposes as of and for the year ended December 31, 2006.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 30, 2007, on our consideration of Valley Mental Health, Incorporated's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audits.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements of Valley Mental Health, Incorporated and Affiliates taken as a whole. The accompanying schedule of expenditures of federal awards of Valley Mental Health, Incorporated (excluding affiliates) for the year ended December 31, 2006, is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic consolidated financial statements taken as a whole.

Tanner LC

April 30, 2007

VALLEY MENTAL HEALTH, INCORPORATED AND AFFILIATES

Consolidated Statements of Financial Position

(Rounded to nearest thousand)

Assets	December 31, 2006	2005
Designated assets:		
Cash and cash equivalents	$ 9,690,000	$ 3,526,000
Marketable securities	10,767,000	18,240,000
Receivables	13,553,000	18,032,000
Advances to an unconsolidated affiliate	2,608,000	2,658,000
Total designated assets	36,618,000	42,456,000
Receivables	4,669,000	769,000
Restricted cash	1,005,000	575,000
Interest in net assets of an unconsolidated affiliate	4,570,000	4,202,000
Land, buildings, and equipment, net	53,808,000	54,453,000
Assets of tax credit housing projects	10,503,000	-
Other assets	2,019,000	2,923,000
Total assets	$ 113,192,000	$ 105,378,000

Liabilities and Net Assets	2006	2005
Accounts payable and accrued liabilities	$ 22,521,000	$ 23,105,000
Note payable	1,438,000	1,880,000
Long-term debt	21,757,000	22,600,000
Liabilities of tax credit housing projects	2,524,000	-
Total liabilities	48,240,000	47,585,000
Commitments and contingencies		
Other owners' interests in consolidated entities	4,492,000	-
Net assets:		
Unrestricted:		
Designated	36,618,000	42,456,000
Undesignated	18,409,000	9,457,000
	55,027,000	51,913,000
Temporarily restricted	4,922,000	5,380,000
Permanently restricted	511,000	500,000
Total net assets	60,460,000	57,793,000
Total liabilities and net assets	$ 113,192,000	$ 105,378,000

See accompanying notes to consolidated financial statements.

VALLEY MENTAL HEALTH, INCORPORATED AND AFFILIATES

Consolidated Statements of Activities

(Rounded to nearest thousand)

	Years Ended December 31, 2006	2005
Unrestricted net assets:		
Revenues and support:		
Medicaid fees	$ 38,933,000	$ 39,289,000
State contract	9,684,000	8,046,000
Other contracts and grants	15,593,000	15,730,000
County contract	6,159,000	6,159,000
Service fees	3,789,000	3,308,000
Revenues of nursing home entities	8,951,000	8,278,000
Flex Care revenue	17,416,000	15,755,000
Other services revenue	2,780,000	2,251,000
Revenues of tax credit housing projects	640,000	-
Increase in interest in net assets of an unconsolidated affiliate	1,490,000	1,100,000
Total unrestricted revenues and support	105,435,000	99,916,000
Expenses:		
Program services:		
Adult services	29,386,000	26,613,000
Children services	25,509,000	24,675,000
Client services	7,951,000	7,796,000
Contract services	3,589,000	3,625,000
Behavioral Health Strategies	521,000	222,000
Flex Care services	16,496,000	15,111,000
Nursing home entities	8,331,000	8,061,000
Housing and building projects	2,933,000	2,043,000
Supporting services:		
Management and general	10,409,000	10,078,000
Total expenses	105,125,000	98,224,000
Increase in unrestricted net assets	310,000	1,692,000
Temporarily restricted net assets-		
Increase (decrease) in interest in net assets of an unconsolidated affiliate	(458,000)	839,000
Permanently restricted net assets-		
Increase in interest in net assets of an unconsolidated affiliate	11,000	-
(Decrease) increase in net assets before other owners' interest in the change in net assets and cumulative effect adjustment	(137,000)	2,531,000
Other owners' interest in the change in net assets	258,000	-
Increase in net assets before cumulative effect change from adoption of a new accouting principle	121,000	2,531,000
Cumulative effect change from adoption of a new accounting principle (see Note 2)	2,546,000	-
Increase in net assets	2,667,000	2,531,000
Net assets, beginning of year	57,793,000	55,262,000
Net assets, end of year	$ 60,460,000	$ 57,793,000

See accompanying notes to consolidated financial statements.

	Program Services			
	Adult Services	Children Services	Client Services	Contract Services
Salaries	$ 13,136,000	$ 12,998,000	$ 4,354,000	$ 1,785,000
Health and retirement benefits	3,245,000	3,731,000	1,465,000	564,000
Payroll taxes, etc.	977,000	1,031,000	380,000	132,000
Total salaries and related expenses	17,358,000	17,760,000	6,199,000	2,481,000
Contracted hospital costs	5,211,000	1,363,000	3,000	551,000
Property and bed taxes	-	-	-	-
Professional fees and contract service payments	3,100,000	2,051,000	27,000	55,000
Assisted living center and other expenses	-	-	-	-
Rent	55,000	-	50,000	10,000
Provisions	591,000	916,000	112,000	42,000
Office operations	375,000	158,000	123,000	34,000
Insurance	171,000	452,000	288,000	38,000
Utilities	477,000	422,000	269,000	74,000
Transportation	239,000	416,000	228,000	60,000
Maintenance	619,000	866,000	379,000	88,000
Education and training	78,000	100,000	27,000	29,000
Reduction in investment in tax credit projects	-	-	-	-
Contributions	-	-	-	-
Expenses of tax credit housing projects	-	-	-	-
Miscellaneous	121,000	2,000	80,000	12,000
Total expenses before depreciation, amortization, and interest expense	28,395,000	24,506,000	7,785,000	3,474,000
Depreciation and amortization	616,000	657,000	164,000	115,000
Interest expense	375,000	346,000	2,000	-
Total expenses	$ 29,386,000	$ 25,509,000	$ 7,951,000	$ 3,589,000

See accompanying notes to consolidated financial statements.

VALLEY MENTAL HEALTH, INCORPORATED AND AFFILIATES

Consolidated Statement of Functional Expenses

(Rounded to nearest thousand)

Year Ended December 31, 2006

Program Services					Supporting Services	
Behavioral Health Strategies	Flex Care Services	Nursing Home Entities	Housing and Building Projects	Total	Management and General	Total
$ -	$ 2,464,000	$ 3,579,000	$ 348,000	$ 38,664,000	$ 4,093,000	$ 42,757,000
-	826,000	3,000	113,000	9,947,000	1,941,000	11,888,000
-	180,000	288,000	28,000	3,016,000	491,000	3,507,000
-	3,470,000	3,870,000	489,000	51,627,000	6,525,000	58,152,000
-	-	1,133,000	-	8,261,000	-	8,261,000
-	-	321,000	-	321,000	-	321,000
435,000	40,000	455,000	9,000	6,172,000	1,891,000	8,063,000
-	11,984,000	-	-	11,984,000	-	11,984,000
-	29,000	76,000	28,000	248,000	4,000	252,000
-	148,000	562,000	1,000	2,372,000	2,000	2,374,000
13,000	128,000	421,000	36,000	1,288,000	659,000	1,947,000
-	9,000	345,000	4,000	1,307,000	41,000	1,348,000
-	170,000	135,000	224,000	1,771,000	204,000	1,975,000
4,000	103,000	6,000	14,000	1,070,000	37,000	1,107,000
1,000	186,000	45,000	703,000	2,887,000	223,000	3,110,000
6,000	4,000	-	5,000	249,000	297,000	546,000
-	-	-	-	-	-	-
-	-	-	-	-	-	-
-	-	-	1,114,000	1,114,000	-	1,114,000
54,000	-	103,000	-	372,000	70,000	442,000
513,000	16,271,000	7,472,000	2,627,000	91,043,000	9,953,000	100,996,000
8,000	224,000	323,000	238,000	2,345,000	431,000	2,776,000
-	1,000	536,000	68,000	1,328,000	25,000	1,353,000
$ 521,000	$ 16,496,000	$ 8,331,000	$ 2,933,000	$ 94,716,000	$ 10,409,000	$ 105,125,000

	Program Services			
	Adult Services	Children Services	Client Services	Contract Services
Salaries	$ 12,979,000	$ 12,832,000	$ 4,428,000	$ 1,750,000
Health and retirement benefits	3,070,000	3,399,000	1,314,000	513,000
Payroll taxes, etc.	958,000	967,000	335,000	124,000
Total salaries and related expenses	17,007,000	17,198,000	6,077,000	2,387,000
Contracted hospital costs	3,640,000	940,000	2,000	631,000
Property and bed taxes	-	-	-	-
Professional fees and contract service payments	2,445,000	2,134,000	103,000	67,000
Assisted living center and other expenses	-	-	-	-
Rent	101,000	-	53,000	7,000
Provisions	572,000	845,000	103,000	48,000
Office operations	300,000	274,000	138,000	56,000
Insurance	174,000	372,000	263,000	37,000
Utilities	422,000	464,000	262,000	78,000
Transportation	210,000	410,000	242,000	53,000
Maintenance	592,000	883,000	327,000	85,000
Education and training	126,000	110,000	21,000	25,000
Reduction in investment in tax credit projects and other entities	-	-	-	-
Contributions	50,000	-	17,000	-
Expenses of tax credit housing projects	-	-	-	-
Miscellaneous	17,000	24,000	8,000	34,000
Total expenses before depreciation, amortization, and interest expense	25,656,000	23,654,000	7,616,000	3,508,000
Depreciation and amortization	626,000	703,000	177,000	117,000
Interest expense	331,000	318,000	3,000	-
Total expenses	$ 26,613,000	$ 24,675,000	$ 7,796,000	$ 3,625,000

See accompanying notes to consolidated financial statements.

VALLEY MENTAL HEALTH, INCORPORATED AND AFFILIATES
Consolidated Statement of Functional Expenses
(Rounded to nearest thousands)

Year Ended December 31, 2005

Program Services					Supporting Services	
Behavioral Health Strategies	Flex Care Services	Nursing Home Entities	Housing and Building Projects	Total	Management and General	Total
$ -	$ 2,257,000	$ 3,149,000	$ 306,000	$ 37,701,000	$ 3,959,000	$ 41,660,000
-	677,000	5,000	95,000	9,073,000	1,884,000	10,957,000
-	166,000	273,000	30,000	2,853,000	504,000	3,357,000
-	3,100,000	3,427,000	431,000	49,627,000	6,347,000	55,974,000
-	-	1,243,000	-	6,456,000	2,000	6,458,000
-	-	243,000	-	243,000	-	243,000
187,000	18,000	438,000	5,000	5,397,000	1,544,000	6,941,000
-	11,183,000	-	-	11,183,000	-	11,183,000
-	27,000	119,000	1,000	308,000	7,000	315,000
-	133,000	620,000	7,000	2,328,000	106,000	2,434,000
13,000	46,000	446,000	36,000	1,309,000	717,000	2,026,000
-	12,000	281,000	43,000	1,182,000	68,000	1,250,000
-	106,000	123,000	191,000	1,646,000	175,000	1,821,000
2,000	84,000	8,000	17,000	1,026,000	38,000	1,064,000
-	195,000	40,000	665,000	2,787,000	254,000	3,041,000
-	3,000	-	23,000	308,000	278,000	586,000
-	-	-	277,000	277,000	-	277,000
-	-	-	-	67,000	-	67,000
-	-	-	-	-	-	-
12,000	4,000	178,000	22,000	299,000	103,000	402,000
214,000	14,911,000	7,166,000	1,718,000	84,443,000	9,639,000	94,082,000
8,000	196,000	317,000	250,000	2,394,000	414,000	2,808,000
-	4,000	578,000	75,000	1,309,000	25,000	1,334,000
$ 222,000	$ 15,111,000	$ 8,061,000	$ 2,043,000	$ 88,146,000	$ 10,078,000	$ 98,224,000

VALLEY MENTAL HEALTH, INCORPORATED AND AFFILIATES
Consolidated Statements of Cash Flows
(Rounded to nearest thousand)

	Years Ended December 31,	
	2006	**2005**
Cash flows from operating activities:		
Increase in net assets	$ 2,667,000	$ 2,531,000
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	2,776,000	2,808,000
Loss on disposition of assets	130,000	22,000
Other owners' interest in the change in net assets	(258,000)	-
Cumulative effect change from adoption of new accounting principle	(2,546,000)	-
Reduction in investment in tax credit projects and other entities	-	287,000
Service revenue in exchange for a vehicle	-	(19,000)
Net increase in interest in net assets of unconsolidated affiliate	(1,043,000)	(1,939,000)
Realized and unrealized (gains) losses on marketable securities	523,000	332,000
Decrease (increase) in:		
Receivables	579,000	(986,000)
Other assets	194,000	(99,000)
Increase (decrease) in:		
Accounts payable and accrued liabilities	(584,000)	1,351,000
Net cash provided by operating activities	2,438,000	4,288,000
Cash flows from investing activities:		
Net decrease (increase) in marketable securities	6,950,000	(4,079,000)
Captial contributions to tax credit projects	-	(113,000)
(Increase) decrease in restricted cash	(430,000)	(48,000)
Purchases of land, buildings and equipment	(1,611,000)	(1,784,000)
Proceeds from sale of assets	8,000	-
Proceeds received from an unconsolidated affiliate	675,000	500,000
(Increase) decrease in advances to an unconsolidated affiliate	50,000	(80,000)
Net cash provided by (used in) investing activities	5,642,000	(5,604,000)
Cash flows from financing activities:		
Proceeds from long-term debt	402,000	352,000
Increase in loan costs included in other assets	-	(71,000)
Net increase (decrease) in note payable	(442,000)	297,000
Payments on long-term debt	(1,876,000)	(3,525,000)
Net cash used in financing activities	(1,916,000)	(2,947,000)
Net increase (decrease) in cash and cash equivalents	6,164,000	(4,263,000)
Cash and cash equivalents at beginning of year	3,526,000	7,789,000
Cash and cash equivalents at end of year	$ 9,690,000	$ 3,526,000

See accompanying notes to consolidated financial statements.

1. Organization and Summary of Significant Accounting Policies

Organization
Valley Mental Health, Incorporated is a Utah not-for-profit corporation which provides and administers mental health, alcohol and drug treatment, and other services principally in the Salt Lake County, Summit County, and Tooele County, Utah areas.

Consolidated Financial Statements
The consolidated financial statements are presented using the accrual method of accounting, and include the accounts of Valley Mental Health, Incorporated and the following affiliated organizations:

- Salt Lake Mental Health Housing, Inc.
- Valley Villa, Inc.
- Valley Crossroads, Inc.

These entities are housing projects constructed using financing obtained through the U.S. Department of Housing and Urban Development (HUD). Valley Mental Health, Incorporated houses clients in each of the apartment projects. These entities are consolidated due to Valley Mental Health, Incorporated's control of the boards of directors of these entities.

- Behavioral Health Strategies, LLC (a West Virginia Limited Liability Company)

This LLC is a 100% owned subsidiary of Valley Mental Health, Incorporated.

- Avalon Valley entities (Avalon Valley)

Avalon Valley consists of Avalon Valley Rehabilitation Center, Inc. (an S Corporation) and Avalon Valley Care Center, LLC. Valley Mental Health, Incorporated acquired a 51% ownership interest in both of these entities to facilitate placement and treatment of certain, difficult to place, mental health clients. No minority interest was reflected in 2005 due to the fact there was a deficit in the combined equity of Avalon Valley and Valley Mental Health, Incorporated is responsible for all liabilities of the combined Avalon Valley entities. During the year ended December 31, 2006, Avalon Valley's equity became positive and therefore, minority interest has been reported.

1. Organization and Summary of Significant Accounting Policies
Continued

- Safe Haven II, LLC
- Valley Horizons, LLC
- Valley Meadows, LLC
- Valley Safe Haven, LLC
- Valley Woods I, L.C.

These limited liability companies are tax credit projects that house clients of Valley Mental Health. As further described in Note 2, these entities are consolidated with Valley Mental Health, Incorporated for 2006 due to the adoption of a new accounting principle.

- Valley Horizons II, LLC

This limited liability company has been organized for the purpose of constructing an additional tax credit housing project. As of December 31, 2006, this entity is wholly owned by Valley Mental Health, Incorporated and construction has not begun.

All material inter-organization transactions and accounts have been eliminated in the consolidation. The consolidated group is referred to as either "VMH" or the "Organization" throughout the remaining notes to consolidated financial statements.

Financial Statement Presentation
The Organization reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Estimates
The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Concentration of Credit Risk
A significant portion of the Organization's revenues and receivables are from government agencies. Receivables from government agencies total $18,351,000 and $18,292,000 at December 31, 2006 and 2005, respectively.

1. Organization and Summary of Significant Accounting Policies
Continued

The Organization maintains cash in bank deposit accounts which generally exceed the $100,000 Federal Deposit Insurance Corporation bank insurance limit. The Organization has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents.

Fair Value of Financial Instruments
The recorded amounts for investments, receivables, accounts payable and accrued liabilities approximate fair value due to the short-term nature of these financial instruments. The fair value of the amount outstanding under the Organization's note payable approximates its recorded value, in all material respects, due to the fact that the note bears interest at a variable market rate. Management's estimate of the fair value of long-term debt, using discounted cash flow analyses based on current borrowing rates for debt with similar maturities and ratings, does not differ materially from the aggregate carrying values of its long-term debt recorded in the accompanying consolidated statements of financial position.

Cash and Cash Equivalents
The Organization considers all unrestricted highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Investments
Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the consolidated statements of financial position. Unrealized gains and losses are included in the change in net assets.

Receivables
Receivables are carried at the original billed amount less an estimate made for potentially uncollectible receivables based on a review of all outstanding amounts on a periodic basis. Management determines the need for an allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Receivables are written off when deemed uncollectible. Recoveries of receivables previously written off are recorded when received.

1. Organization and Summary of Significant Accounting Policies *Continued*

Interest in Net Assets of and Advances to Other Organizations
VMH accounts for transfers of assets to other nonprofit organizations meeting specified criteria by applying the provisions of Statement of Financial Accounting Standards No. 136 "Transfers of Assets to a Not-For-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others" (SFAS No. 136). Under the provisions of SFAS No. 136, VMH recognizes an interest in the net assets of the other nonprofit organizations and in the changes in net assets of the other nonprofit organizations. VMH recognizes "Advances to an unconsolidated affiliate" for funds transferred from VMH to other nonprofit organizations for which VMH expects repayment in the future to support its programs.

Restricted Cash
Restricted cash represents loan proceeds intended for the construction of Valley Horizons II, LLC and cash accounts held by affiliates in accordance with operating agreements or HUD requirements.

Land, Buildings and Equipment
The Organization capitalizes purchases of land, buildings and equipment at cost. The fair value of donated land, buildings and equipment is similarly capitalized. Minor replacements, maintenance and repairs, which do not increase the useful lives of the property, are expensed as incurred. Depreciation and amortization are provided on a straight-line basis over the estimated useful lives of the assets or lease terms.

Investments in Unconsolidated Affiliates
The Organization has a non-controlling ownership interest in certain companies. When the Organization's ownership is less than 20%, the investment is recorded using the cost method of accounting, and when ownership is 20% or more, the investment is accounted for using the equity method. Investments in such companies are included under the caption "Other Assets" in the consolidated statements of financial position.

Impairment of Long-Lived Assets
VMH reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable through undiscounted future cash flows. If it is determined that an impairment loss has occurred based on expected cash flows, such loss is recognized in the consolidated statement of activities.

1. Organization and Summary of Significant Accounting Policies
Continued

Revenue Recognition
Service revenue is recognized in accordance with the terms of service contracts and as service is provided. Generally, revenue is recognized when services have been performed, and collection is reasonably assured.

Rental revenue is recognized proportionately over the rental term and when collection is reasonably assured. Rent collected in advance is recorded as deferred revenue until earned

Contributions
Contributions received, if any, are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions.

Donated Property and Equipment
Donations of property and equipment are recorded as support at their estimated fair value at the date of donation. Such donations are reported as unrestricted support unless the donor has restricted the donated asset to a specific purpose. Assets donated with explicit restrictions regarding their use and contributions of cash that must be used to acquire property and equipment are reported as restricted support. Absent donor stipulations regarding how long those donated assets must be maintained, the Organization reports expirations of donor restrictions when the donated or acquired assets are placed in service as instructed by the donor. The Organization reclassifies temporarily restricted net assets to unrestricted net assets at that time.

1. Organization and Summary of Significant Accounting Policies
Continued

Donated Services

Donated services are recognized as contributions if the services (a) create or enhance non-financial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by VMH. Many individuals volunteer their time and perform a variety of tasks that assist the Organization with specific programs and assignments, however, the services do not meet the above criteria.

Income Tax Status

The Organization is a qualified charitable organization under Section 501(c)(3) of the Internal Revenue Code and under State of Utah regulations, and as such, is not subject to federal or state income taxes on related business income. The Organization is subject to taxation on unrelated business income.

The Organization's ownership interest in Avalon Valley Rehabilitation Center, Inc. (an S Corporation) subjects the Organization to unrelated business income tax on allocations of profit from Avalon Valley Rehabilitation Center, Inc. Estimated income taxes pertaining to VMH's portion of the taxable income are not material, therefore, no provision for income taxes has been recorded.

Expense Allocation

The costs of providing various programs and other activities have been summarized on a functional basis in the consolidated statements of activities and in the consolidated statements of functional expenses. Accordingly, certain indirect costs have been allocated among the programs and supporting services benefited.

Reclassification

Certain amounts in the 2005 consolidated financial statements have been reclassified to conform with the current year presentation.

2. Adoption of New Accounting Pronouncement

Effective January 1, 2006, the Organization was required to implement the provisions of Emerging Issues Task Force Issue No. 04-5 (EITF 04-5) *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights.* Under the provisions of EITF 04-5 the general partners are presumed to control a limited partnership (or a limited partnership equivalent entity) regardless of the extent of the general partners' ownership interest. The assessment of whether the rights of the limited partners should overcome the presumption of control by the general partners is a matter of judgment that depends on whether the limited partners have either (a) the substantive ability to liquidate the limited partnership or otherwise remove the general partners without cause or (b) substantive participating rights. Substantive participating rights provide the limited partners with the ability to effectively participate in significant financial and operating decisions that would be expected to be made in the ordinary course of the limited partnership's business.

Management has determined that under EITF 04-5, Valley Mental Health, Incorporated is deemed to control the low-income housing tax credit projects listed below. Therefore, these entities have been consolidated in the accompanying consolidated financial statements beginning January 1, 2006.

- Safe Haven II, LLC
- Valley Horizons, LLC
- Valley Meadows, LLC
- Valley Safe Haven, LLC
- Valley Woods I, L.C.

Prior to January 1, 2006, the Organization did not consolidate these tax credit housing projects because the limited partners were deemed to have "important rights" under the provisions of Statement of Position 78-9. As permitted by EITF 04-5, management implemented the effect of this pronouncement on the consolidated financial statements by recording a cumulative-effect-type adjustment effective January 1, 2006, totaling $2,546,000, that increased net assets.

2. Adoption of New Accounting Pronouncement *Continued*

As of December 31, 2006, the Organization had recorded the following related to tax credit housing projects in the consolidated statement of financial position: (1) assets of $10,503,000 (primarily land, buildings and equipment); (2) liabilities of $2,524,000, including long-term debt, of which $66,000 is due by December 31, 2007; (3) other owners' interest in tax credit housing projects of $4,365,000, which is part of "other owners' interests in consolidated entities"; and (4) net assets of $3,614,000. The consolidated statement of activities for the year ended December 31, 2006, includes the following related to the tax credit housing projects: (1) Revenues of $640,000; (2) expenses of $1,114,000; and (3) other owners' interest in the change in net assets of $470,000.

3. Marketable Securities

Marketable securities are stated at fair market value and consist of the following:

	December 31,	
	2006	2005
Treasury notes and other government securities	$ 10,592,000	$ 18,240,000
Corporate fixed income securities	175,000	-
	$ 10,767,000	$ 18,240,000

Investment return is summarized as follows for the years ended December 31:

	2006	2005
Interest income, net of fees	$ 657,000	$ 540,000
Net realized and unrealized gains (losses)	(523,000)	(332,000)
	$ 134,000	$ 208,000

4. Detail of Certain Balances

Receivables	December 31, 2006	December 31, 2005
Cost reimbursement and fee-for-service contracts with government agencies	$ 12,602,000	$ 14,797,000
Receivables from clients, insurance companies and other non-government agencies, net of an allowance for doubtful accounts of $81,000 and $84,000, respectively	5,130,000	3,720,000
Related party receivables	490,000	284,000
	$ 18,222,000	$ 18,801,000

Accounts Payable and Accrued Liabilities	December 31, 2006	December 31, 2005
Contract related liabilities	$ 10,175,000	$ 12,585,000
Accrued payroll taxes and other benefits	4,865,000	4,327,000
Accrued vacation and sick pay	2,782,000	2,568,000
Trade accounts payable	2,140,000	2,379,000
Fair value of interest rate swap	236,000	244,000
Other accrued liabilities	2,323,000	1,002,000
	$ 22,521,000	$ 23,105,000

5. Interest In and Advances to an Unconsolidated Affiliate

The Organization has an affiliate, Valley Mental Health Foundation, Inc. (the Foundation), that does not meet the criteria to be consolidated. The "Interest in net assets of unconsolidated affiliate" represents VMH's interest in the net assets of the Foundation. "Advances to an unconsolidated affiliate" represents amounts transferred from VMH to the Foundation which will either be returned to VMH or used for VMH programs. VMH does not grant variance power to the Foundation.

5. Interest In and Advances to an Unconsolidated Affiliate ***Continued***

VMH's consolidated financial statements reflect the following with respect to the Foundation as of December 31:

	2006	2005
Advances to an unconsolidated affiliate	$ 2,608,000	$ 2,658,000
Interest in the net assets of unconsolidated affiliate	4,570,000	4,202,000
	$ 7,178,000	$ 6,860,000

VMH recognized the following in its consolidated statements of activities with respect to the Foundation for the years ended December 31:

	2006	2005
Increase in interest in the unrestricted net assets of an unconsolidated affiliate	$ 1,490,000	$ 1,100,000
Increase (decrease) in interest in the temporarily restricted net assets of an unconsolidated affiliate	(458,000)	839,000
Increase (decrease) in interest in the permanently restricted net assets of an unconsolidated affiliate	11,000	-
	$ 1,043,000	$ 1,939,000

6. Land, Buildings and Equipment

Land, buildings and equipment consist of the following at December 31:

	2006	2005
Land	$ 10,837,000	$ 10,837,000
Land improvements	1,068,000	1,039,000
Buildings and improvements	49,147,000	49,133,000
Leasehold improvements	4,279,000	3,095,000
Office furniture and equipment	9,091,000	8,364,000
Automobiles and trucks	1,740,000	1,814,000
Construction in progress	259,000	224,000
Total cost	76,421,000	74,506,000
Less accumulated depreciation and amortization	(22,613,000)	(20,053,000)
	$ 53,808,000	$ 54,453,000

7. Note Payable

Avalon Valley Care Center, LLC has a $2,000,000 unsecured line of credit agreement with a bank. As of December 31, 2006 and 2005, Avalon Valley had borrowed $1,438,000 and $1,880,000, respectively, under the agreement. The agreement expires on October 1, 2010. The interest rate is half a percent above the prime rate (8.75% at December 31, 2006). The line of credit is guaranteed by members of Avalon Valley Care Center, LLC. As of December 31, 2006, the Organization was out of compliance with a loan covenant related to this note payable. The loan covenant requires the Organization to attain a minimum annual increase in net assets. The bank has granted a waiver of this loan covenant.

8. Long-term Debt

Long-term debt consists of the following at December 31:

	2006	2005
Loan payable (see note 9)	$ 13,830,000	$ 14,445,000
Mortgage note payable by Avalon Valley Rehabilitation Center, Inc. to a financial institution. Due in monthly payments of $37,127, including interest at 6.375%. The note matures in August 2039, is secured by real property and insured by HUD.	6,113,000	6,167,000
Mortgage note payable, bearing interest at the LIBOR rate plus 1.75% (6.25% at December 31, 2005), payable in monthly installments of $3,438, secured by real property. The note was paid-in-full in April 2006.	-	825,000
Mortgage note payable by a consolidated affiliate to HUD with an interest rate of 9.25%, due in 2028, payable in monthly installments of $6,570, secured by real property.	731,000	742,000
Construction loan payable by a consolidated affiliate, bearing interest at the LIBOR rate (5.36% at December 31, 2006), payable when permanent funding for construction purposes is established.	402,000	-

8. Long-term Debt
Continued

	2006	2005
Note payable to a company, due in annual installments of approximately $41,000 including interest at 7%, secured by real estate	40,000	76,000
Capital lease obligations (see note10)	641,000	345,000
	$ 21,757,000	$ 22,600,000

Future maturities are as follows:

Years Ending December 31:	
2007	$ 1,406,000
2008	998,000
2009	921,000
2010	840,000
2011	873,000
Thereafter	16,719,000
	$ 21,757,000

9. Loan Payable and Interest Rate Swap

During the year ended December 31, 2001, VMH entered into agreements to obtain funding to construct two new buildings. Funding was made available to VMH through Salt Lake City (the City) by the City's issuance of Variable Rate Revenue Bonds (the Bonds). Proceeds from the sale of the Bonds by the City were loaned to VMH under the terms of a loan agreement.

Concurrent with the issuance of the Bonds, VMH delivered to a trustee an irrevocable letter of credit to secure repayment of the bond proceeds. Under the letter of credit, the trustee has the ability to draw an amount sufficient to pay the principal of the Bonds and up to 45 days of accrued interest. The initial term of the letter of credit expires December 2008. The letter of credit is secured by land and buildings.

9. Loan Payable and Interest Rate Swap *Continued*

Interest on the loan to VMH is equivalent to the interest rate on the associated bonds issued by the City. As of December 31, 2006, the interest rate was being set weekly. The interest rate at December 31, 2006 and 2005 was 4.25% and 3.38%, respectively. The loan matures December 2021. Annual mandatory principal payments are due December 1 each year. The amount outstanding as of December 31, 2006 and 2005 was $13,830,000 and $14,445,000, respectively.

Interest Rate Swap

During the year ended December 31, 2004, VMH entered into an interest rate swap to obtain a fixed rate on its variable-rate loan from the City. The total notional amount of the swap is $7,515,000 at December 31, 2006 and 2005. This cash flow hedge changes the variable-rate interest on the notional amount of VMH's bonds to a fixed-rate interest. Under the terms of the swap (which expires June 1, 2014), VMH pays monthly a fixed interest rate of 4.25%. VMH receives monthly the floating variable interest rate based upon the weekly interest rate resets of tax-exempt variable rate issues on the interest rate swap. The estimated fair value of this swap agreement at December 31, 2006 and 2005 was a liability of approximately $236,000 and $244,000, respectively, which is included in accounts payable and other accrued liabilities.

As there are no differences between the critical terms of the interest rate swap and the hedged debt obligation, VMH assumes no ineffectiveness in the hedging relationship.

10. Capital Lease Obligations

VMH leases certain equipment and fixtures under noncancellable leases that meet the criteria to be accounted for as capital leases. Assets under these capital leases included in land, buildings and equipment are as follows as of December 31, 2006:

Office furniture and equipment	$ 1,374,000
Less accumulated amortization	(758,000)
	$ 616,000

Amortization expense for assets under capital leases during the years ended December 31, 2006 and 2005 was $336,000 and $144,000, respectively.

10. Capital Lease Obligations *Continued*

The capital lease obligations have imputed interest rates ranging from 5% to 11%, are payable in aggregate monthly installments of approximately $40,000, and mature January 2007 through November 2011. The leases are secured by equipment. Future minimum payments on the capital lease obligations are as follows:

Years Ending December 31:	Amount
2007	$ 278,000
2008	260,000
2009	133,000
2010	11,000
2011	2,000
	684,000
Less amount representing interest	(43,000)
Present value of future minimum lease payments	$ 641,000

11. Designation of Unrestricted Net Assets

The Board of Trustees has designated a portion of VMH's unrestricted net assets, and an equal amount of cash and cash equivalents, marketable securities, receivables, and advances to an unconsolidated affiliate, to provide for replacement and upgrade of furnishings and equipment, payment of Medicaid related liabilities, ninety days of working capital, repayment of a portion of the loan from the city, and for certain programs.

12. Restrictions on Net Assets

Temporarily Restricted

Temporarily restricted net assets are available for the following purposes at December 31:

	2006	2005
HUD capital advances to Valley Villa, Inc. and Valley Crossroads, Inc.	$ 2,288,000	$ 2,288,000
CBTU/Autism	1,709,000	2,027,000
Safe Haven/Homeless	828,000	927,000
Other	97,000	138,000
	$ 4,922,000	$ 5,380,000

12. Restrictions on Net Assets *Continued*

***Temporarily Restricted** - Continued*

No repayment of capital advances is required and no interest will accrue so long as the apartments owned by Valley Villa, Inc. and Valley Crossroads, Inc. remain available for low-income persons with disabilities in accordance with Section 811 of the Affordable Housing Act of 1990, and the regulatory agreements with HUD.

Provided that the housing has remained available for occupancy by eligible families until the maturity date of the capital advance notes (September 2035 for Valley Villa, Inc. and April 2037 for Valley Crossroads, Inc.) and the notes have not otherwise become due and payable by reason of default under the notes or regulatory agreements, the notes shall be deemed to be paid and discharged on the maturity date.

In the event of default, the entire balance can be declared due and payable by HUD, and interest would be accrued from the date of the initial capital advances received.

Permanently Restricted

Permanently restricted net assets of $500,000 represent a general endowment fund held by Valley Mental Health Foundation, Inc. The endowment principal is to be retained and invested. The earnings from the $500,000 endowment are available for unrestricted use by Valley Mental Health, Foundation, Inc. Permanently restricted net assets of $11,000 as of December 31, 2006, represent an endowment fund for services to children.

13. Contracts

VMH has entered into agreements with Salt Lake County, Summit County, and Tooele County, Utah (the Counties) to provide substantially all of the mental health services which are required to be provided by the Counties. In addition, VMH has agreements to provide substantially all alcohol and drug treatment services in Summit and Tooele Counties and a portion of those services in Salt Lake County. Under the terms of these agreements, VMH provides certain mutually agreed upon mental health and alcohol and drug treatment services in exchange for fees which are mutually negotiated annually based on VMH's costs and other revenue sources. The Counties have also assigned to VMH their interest in various contracts with other governmental agencies to provide these services.

14. Retirement Plans

The Organization makes contributions to a multi-employer defined benefit retirement plan administered by the Utah State Retirement Fund (the Plan). These contributions are determined in accordance with provisions of the Plan. Information as to the Organization's portion of the accumulated Plan benefits, Plan net assets and unfunded vested benefits is not determinable. In the event of withdrawal from the Plan, the Organization may be subject to payment of a withdrawal liability. Management does not intend to take any action which would subject it to such liability. Also, Utah State law only allows withdrawals under certain limited circumstances.

In addition to the above plan, the Organization has defined contribution retirement plans covering eligible employees. These plans are funded by employee contributions and, for one plan, contributions are made by the Organization at a set percent of the participating employees' compensation.

The Organization contributed approximately $4,600,000 to the above described plans during each of the years ended December 31, 2006 and 2005.

15. Post-Retirement Benefit

VMH provides post-retirement medical insurance benefits for employees and their dependents who have retired from VMH, qualify under the provisions of the post-retirement benefit plan, and are under the age of 65. The benefit is terminated once the retiree reaches the age of 65, and terminates for the employee's spouse once he/she reaches the age of 65. The retiree is responsible for a portion of the insurance premium.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard No. 158 (SFAS 158). The statement requires an employer to:

- Recognize the funded status of a benefit plan, measured as the difference between plan assets at fair value and the benefit obligation, in its statement of financial position.

15. Post-Retirement Benefit
Continued

- Recognize the gains or losses and prior service costs or credits, net of tax, that arise during the period but are not recognized as components of net periodic benefit cost pursuant to FASB Statement No. 87, *Employers Accounting for Pensions,* or No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions.*

The adoption date required for VMH is the first fiscal year ending after June 15, 2007. VMH plans to adopt this standard for the year ended December 31, 2007.

The following tables provide information relating to the postretirement benefit plan as of and for the years ended December 31,:

	2006	2005
Benefit obligation	$ 3,919,000	$ 3,727,000
Fair value of plan assets	$ -	$ -
Funded status	$ (3,919,000)	$ (3,727,000)
Accrued benefit cost recognized in the consolidated statements of financial position as part of accounts payable and accrued liabilities	$ 1,836,000	$ 1,487,000
Benefit cost	$ 555,000	$ 501,847
Participant contributions	$ 217,000	$ 87,184
Employer contributions	$ 207,000	$ 176,638
Benefits paid	$ 392,000	$ 237,230

Weighted average assumptions for net benefit costs as of December 31,:

	2006	2005
Discount rate	5.50%	5.75%
Expected return on plan assets	N/A	N/A
Rate of compensation increase	N/A	N/A

15. Post-Retirement Benefit
Continued

Weighted average assumptions for benefit obligations as of December 31,:

	2006	2005
Discount rate	5.75%	5.50%
Rate of compensation increase	N/A	N/A
Rate of compensation increase	N/A	N/A

Assumed health care cost trends as of December 31,:

	2006	2005
Health care cost trend assumed for next fiscal year	10.00%	10.00%
Average rate to which the cost trend is assumed to decline (ultimate trend rate)	.80%	.75%
Year that the rate reaches the ultimate trend rate	2012	2013

The Organization expects to contribute $220,000 to the post retirement benefit plan in 2007.

Estimated future benefit payments:

Years Ending December 31,:	Amount
2007	$ 348,000
2008	411,000
2009	518,000
2010	570,000
2011	596,000
2012	3,437,000
Total	$ 5,880,000

16. Commitments and Contingencies

Long Term Contracts
VMH has entered into numerous agreements with government and private agencies to provide mental health and other services. The terms of these agreements may require adjustments to be made to revenues received based on events which are not currently determinable. The amount of these adjustments, if any, is also not currently estimable. Such adjustments could be material to the consolidated financial statements.

Litigation
In the normal course of operations, VMH may become party to claims and/or lawsuits. The amount, if any, to be paid by VMH in connection with this litigation is not estimable and the likelihood of an unfavorable outcome is not currently determinable. Management believes damages (if any) resulting from claims are adequately insured and will not have a material adverse effect on the Organization's financial position.

Contract Guarantees Related to Tax Credit Projects
Under the terms of operating agreements for the tax credit housing projects, VMH has agreed to reimburse the investor member of the projects for shortfalls in tax credits obtained for the project in comparison to projected tax credits, and to provide certain loans for operating deficits, if needed. The regulations related to tax credit projects are complex. Noncompliance with these regulations may result in the loss of tax credits associated with a project. VMH is not aware of noncompliance that would result in a reduction of tax credits at this time.

Operating Leases
The Organization leases property under operating leases. Minimum future rental payments due under non-cancelable operating leases are approximately as follows:

16. Commitments and Contingencies *Continued*

***Operating Leases** – Continued*

Years Ending December 31,:		
2007	$	57,000
2008		43,000
2009		16,000
2010		16,000
2011		-
	$	132,000

Rent expense related to these non-cancelable operating leases was approximately $91,000 and $191,000 for the years ended December 31, 2006 and 2005, respectively.

Management Agreement

The Avalon Valley nursing home entities pay a monthly accounting and data processing fee, which is adjusted annually. In addition, they pay a management fee to a management company owned by certain shareholders and members of the Avalon Valley nursing home entities. These fees are adjusted annually and are due under a management agreement that expires September 30, 2010. In addition, they pay a management fee equal to 4% of the adjusted gross patient revenues of the facility. The fees totaled approximately $362,000 and $340,000, respectively, for the years ended December 31, 2006 and 2005.

17. Supplemental Disclosure of Cash Flow Information

During the year ended December 31, 2006:

- VMH acquired property and equipment with proceeds from a capital lease in the amount of $631,000

- VMH consolidated certain tax credit housing projects in accordance with EITF 04-5, which resulted in a cumulative effect adjustment increasing net assets by $2,546,000. The other owners' of the tax credit projects recognized a loss of $470,000 during the year ended December 31, 2006. The Organization reclassified investments totalling $683,000 in these tax credit housing projects previously classified under the caption "other assets" on the statement of financial position. As of December 31, 2006, the Organization had recorded the following relative to the tax credit housing projects: (1) assets of $10,503,000 (2) liabilities of $2,524,000 and (3) other owners' interests in consolidated entities of $4,365,000.

- The other owners of the nursing home entities recognized an increase in their ownership interests of $127,000.

During the year ended December 31, 2005:

- VMH acquired land and a building with proceeds from long-term debt in the amount of $825,000

- VMH acquired equipment in the amount of $19,000 in exchange for tuition revenue.

Amounts paid for:

	Years Ended December 31, 2006	Years Ended December 31, 2005
Interest	$ 1,315,000	$ 1,314,000
Income taxes	$ -	$ -

18. Related Party Transactions

The Organization has entered into a number of related party transactions with the following entities:

Valley Mental Health Foundation, Inc. (the Foundation), a Utah not-for-profit corporation organized to raise funds for Valley Mental Health, Incorporated's programs and facilities. Certain board members of the Foundation are members of the Valley Mental Health, Incorporated board or management. The following transactions occurred during the years ended December 31, 2006 and 2005:

- Valley Mental Health, Incorporated paid the salary and benefits of an individual who works exclusively for the Foundation as well as certain other costs of the Foundation totaling approximately $104,000 and $111,000 for the years ended December 31, 2006 and 2005, respectively;

- The Foundation transferred to Valley Mental Health, Incorporated, for support of its programs, approximately $726,000 and $694,000 for the years ended December 31, 2006 and 2005, respectively;

- Valley Mental Health, Incorporated had receivables totaling $419,000 and $271,000 from the Foundation at December 31, 2006 and 2005, respectively, included in related party receivables.

Valley Services, Inc. is a Utah not-for-profit corporation established primarily to employ Valley Mental Health, Incorporated clients in buildings and grounds maintenance and other services. Certain Valley Mental Health, Incorporated board members and/or management are also members of the board of Valley Services, Inc. However, Valley Mental Health, Incorporated does not control a majority of board appointments. The following related party transactions occurred during the years ended December 31, 2006 and 2005:

18. Related Party Transactions
Continued

Valley Services, Inc. – *Continued*

- Total expenses recognized in 2006 and 2005 for services provided to VMH are approximately $2,388,000 and $2,645,000, respectively;

- One employee of Valley Services, Inc. is a current board member of VMH;

- Accounts payable and accrued liabilities to Valley Services, Inc., as of December 31, 2006 and 2005, are approximately $1,005,000 and $302,000, respectively;

- Valley Services paid Valley Mental Health, Incorporated rent of approximately $48,000 and $40,000, respectively, for 2006 and 2005, for lease of facilities during those years;

- Valley Mental Health, Incorporated has a contract with the Utah Department of Workforce Services in which Valley Mental Health, Incorporated contracted with Valley Services to perform the required services. For the years ended December 31, 2006 and 2005, Valley Mental Health, Incorporated paid Valley Services approximately $109,000 and $102,000, respectively.

Valley Woods I, L.C., (Valley Woods) is a Utah limited liability company which owns a housing project that is used to house Valley Mental Health, Incorporated clients. Under the terms of an operating agreement with the investor member of Valley Woods, Valley Mental Health, Incorporated shares in profits and losses at a rate of 1%. The project takes advantage of low income housing tax credits. These credits are utilized by the investor member of Valley Woods. Once the tax credits have been fully utilized, Valley Mental Health, Incorporated may have the option to acquire the interest of the investor member. Valley Mental Health, Incorporated acts as the managing member of Valley Woods, and receives a management agent fee. Under the requirements of EITF 04-5, as described in Note 2, Valley Mental Health, Incorporated was required to consolidate Valley Woods I, L.C. for financial reporting purposes beginning January 1, 2006. The following related party transactions occurred during the year ended December 31, 2005:

18. Related Party Transactions
Continued

Valley Woods I, L.C. – *Continued*

- In 2005 Valley Mental Health, Incorporated made a capital contribution of $20,000, for the purpose of subsidizing this project due to certain required maintenance to maintain the project in proper condition. Maintenance costs, at times exceed anticipated levels due to the unique tenant population;

- Valley Mental Health, Incorporated received a management agent fee of approximately $24,000 for the year ended December 31, 2005;

- Other assets as of December 31, 2005, include an amount representing VMH's investment interest totaling approximately $87,000;

- During the year ended December 31, 2005, VMH incurred expenses on behalf of Valley Woods I, L.C. of approximately $8,000 for property insurance;

- Valley Mental Health, Incorporated paid Valley Woods, approximately $12,000 during the year ended December 31, 2005, for rent subsidy for patients of VMH.

Valley Mental Health, Incorporated has a .75% profit and loss sharing interest in two Utah limited liability companies; **Hidden Oaks V, L.C.**, and **Iron Horse Park, L.C.** (the Projects). Both of these Projects operate low income housing apartments. These Projects have been awarded low-income housing tax credits which are utilized by the 99% owner of the Projects. VMH may have the option to acquire a majority interest in the Projects once the tax credits have been fully utilized. VMH plans to use future anticipated cash flows, if any, from these Projects to provide funds for mental health services.

18. Related Party Transactions *Continued*

Hidden Oaks V, L.C. and Iron Horse Park, L.C. – *Continued*

- Valley Mental Health, Incorporated has a note receivable from Hidden Oaks V, LC totaling approximately $373,000 and $372,000 as of December 31, 2006 and 2005, respectively, with accrued interest receivable at December 31, 2006 and 2005, of approximately $518,000 and $450,000, respectively. These totals are included in other assets. The note receivable requires payment in full in 2013, bears interest at 8%, and is secured by real property;

- Valley Mental Health, Incorporated recognized interest income of approximately $68,000 and $63,000 related to the above note receivable during the years ended December 31, 2006 and 2005, respectively.

Valley Mental Health, Incorporated has a .5% profit and loss sharing interest in **Valley Meadows, LLC**, a Utah limited liability company. Valley Meadows owns low income housing apartments in Tooele County. This project has been awarded low income housing tax credits which will be utilized by the 99% owner of Valley Meadows. Valley Mental Health, Incorporated may have the option to acquire a majority interest in Valley Meadows, LLC once the tax credits have been fully utilized. Valley Mental Health, Incorporated plans to use future anticipated cash flows, if any, from this project to provide funds for mental health services. Under the requirements of EITF 04-5, as described in Note 2, Valley Mental Health, Incorporated was required to consolidate Valley Meadows, LLC for financial reporting purposes beginning January 1, 2006. The following transactions occurred during the year ended December 31, 2005:

- In 2005, Valley Mental Health, Incorporated made a capital contribution of $33,000 for the purpose of subsidizing this project due to certain required maintenance to maintain the project in proper condition. Maintenance costs, at times exceed anticipated levels due to the unique tenant population;

- Other assets include an amount representing Valley Mental Health, Incorporated's investment totaling approximately $179,000 as of December 31, 2005.

18. Related Party Transactions
Continued

Valley Mental Health, Incorporated has a 1% profit and loss sharing interest in **Valley Safe Haven, LLC**, (Safe Haven) a Utah limited liability company. Safe Haven owns a facility used by Valley Mental Health, Incorporated in serving its clients. The project has taken advantage of low income housing tax credits. These credits will be utilized by the investor member of Safe Haven. Once the tax credits have been fully utilized, Valley Mental Health, Incorporated may have the option to acquire the interest of the investor member. Under the requirements of EITF 04-5, as described in Note 2, Valley Mental Health, Incorporated was required to consolidate Valley Safe Haven, LLC for financial reporting purposes beginning January 1, 2006. The following transactions occurred during the years ended December 31, 2005:

- Valley Mental Health, Incorporated made a capital contribution of $45,000 to Safe Haven during the year ended December 31, 2005, for the purpose of subsidizing this project due to certain required maintenance to maintain the project in proper condition. Maintenance costs, at times exceed anticipated levels due to the unique tenant population;

- A portion of Salt Lake County's appropriation to Valley Mental Health, Incorporated for 2005 was granted to Safe Haven. The total grant for each year was $40,000, which was paid in cash during each year;

- Valley Mental Health, Incorporated received a management agent fee of approximately $16,000 for 2005;

- Valley Mental Health, Incorporated paid Safe Haven rent of $18,000 to lease office space for 2005;

- During the year ended December 31, 2005, VMH incurred expenses on behalf of Valley Safe Haven, LLC of approximately $5,000 for property insurance;

- Other assets as of December 31, 2005, include an amount representing Valley Mental Health, Incorporated's investment totaling approximately $48,000.

18. Related Party Transactions
Continued

Valley Safe Haven, LLC – *Continued*

Guarantee
If an operating deficit exists then Valley Mental Health, Incorporated is required to make an operating deficit loan in the amount of such deficit. The loan will be a subordinated loan, bear interest, and be repaid. As of December 31, 2005, no amounts had been advanced as operating deficit loans.

Valley Mental Health, Incorporated has a .01% profit and loss sharing interest in **Valley Horizons, LLC**, a Utah limited liability company. Valley Horizons owns a facility used by VMH in housing its clients. This project has been awarded low income housing credits which will be utilized by the 99.9% profit and loss sharing interest holder of Valley Horizons. Once the tax credits have been fully utilized, VMH may have the option to acquire the interest of the investor member. Under the requirements of EITF 04-5, as described in Note 2, Valley Mental Health, Incorporated was required to consolidate Valley Horizons, LLC for financial reporting purposes beginning January 1, 2006. The following related party transactions occurred during the year ended December 31, 2005:

- Valley Mental Health, Incorporated received a management fee in 2005 of approximately $23,000 for the benefit of subsidizing this project due to certain requirements to maintain the project in proper order;

- Valley Mental Health, Incorporated paid tenant assistance payments for patients of VMH of approximately $5,000 during the year ended December 31, 2005;

- Other assets, as of December 31, 2005, include an amount representing Valley Mental Health, Incorporated's investment totaling approximately $177,000.

18. Related Party Transactions *Continued*

Valley Horizons, LLC – *Continued*

Guarantee

Based on the operating agreement of Valley Horizons, Valley Mental Health, Incorporated may be required to make an operating deficit contribution. If an operating deficit exists which is not funded from an operating reserve of Valley Horizons, then, Valley Mental Health, Incorporated is required to make a capital contribution in an amount equal to the amount of the operating deficit (Valley Mental Health, Incorporated's maximum exposure is $500,000). The obligation to make these contributions will terminate when all of the following have occurred: (i) Valley Horizons operates at a "break-even" for at lease five consecutive years; (ii) the combined balance in the Operating Reserve of Valley Horizons equals $22,000 (as of December 31, 2005 this balance was approximately $22,000); and (iii) Valley Horizons has achieved the required debt service coverage for the immediately preceding thirty-six months. Any Operating Deficit contributions are repayable, without interest.

Valley Mental Health, Incorporated has a 1% profit and loss sharing interest in **Safe Haven II, LLC**, a Utah limited liability company. Safe Haven II owns a facility used by Valley Mental Health, Incorporated in housing its clients. The project has taken advantage of low income housing tax credits. Once the tax credits have been fully utilized, Valley Mental Health, Incorporated may have the option to acquire the interest of the investor member. Under the requirements of EITF 04-5, as described in Note 2, Valley Mental Health, Incorporated was required to consolidate Safe Haven II, LLC for financial reporting purposes beginning January 1, 2006. The following related party transactions occurred during the year ended December 31, 2005:

- Valley Mental Health, Incorporated received a management fee of $17,000 during the year ended December 31, 2005;

- Valley Mental Health, Incorporated paid Safe Haven II, approximately $46,000 during the year ended December 31, 2005, for rent subsidy for clients living in the facility that were unable to pay their full rent;

18. Related Party Transactions *Continued*

Safe Haven II, LLC – *Continued*

- Valley Mental Health, Incorporated paid expenses in the amount of $8,500 during the year ended December 31, 2005;

- Other assets as of December 31, 2005, include an amount representing Valley Mental Health, Incorporated's investment totaling approximately $456,000.

Guarantee
If an operating deficit exists then Valley Mental Health, Incorporated is required to make an operating deficit loan in the amount of such deficit. The loan will be a subordinated loan, bear interest, and be repaid. As of December 31, 2005, no amounts had been advanced as operating deficit loans.

Valley Mental Health, Incorporated is a member of the **Utah Behavioral Health Network** (UBHN) and a key employee of Valley Mental Health, Incorporated serves on the board of UBHN. During the years ended December 31, 2006 and 2005, the following transactions occurred:

- Valley Mental Health, Incorporated paid membership fees of approximately $83,000 and $82,000, respectively;

- Valley Mental Health, Incorporated paid maintenance of effort payments to UBHN of $323,000 and $396,000, respectively;

- Certain employees of UBHN are included in the Valley Mental Health, Incorporated payroll system. These costs are reimbursed by UBHN.

Valley Mental Health, Incorporated is a member of **Mental Health Risk Retention Group** (MHRRG), a captive insurance company for not-for-profit mental health programs. A key employee of Valley Mental Health, Incorporated serves as a board member of MHRRG. The following related party transactions occurred during the years ended December 31, 2006 and 2005:

18. Related Party Transactions
Continued

MHRGG – *Continued*

- Valley Mental Health, Incorporated obtained its liability insurance coverage from MHRRG. Valley Mental Health, Incorporated paid premiums to MHRRG during 2006 and 2005, of approximately $407,000;

- During 2006 and 2005, Valley Mental Health, Incorporated received dividend income from MHRRG of approximately $42,000 and $41,000, respectively;

- A key employee of Valley Mental Health, Incorporated who serves on the board of MHRRG, receives $1,000 a year as compensation for his service on that board.

A key employee serves as a board member of **Pioneer Behavioral Health (PBH),** a national healthcare company which specializes in behavioral health services. PBH leases space from VMH. During the years ended December 31, 2006 and 2005, VMH recognized rent revenue of approximately $259,000.

Valley Mental Health, Incorporated has certain agreements with companies owned by employees or close relatives of employees to provide services to Valley Mental Health, Incorporated. During the years ended December 31, 2006 and 2005, Valley Mental Health, Incorporated paid these companies approximately $660,000 and $547,000, respectively.

19. Summarized Financial Data For Certain Unconsolidated Affiliates

Following is a summary of financial data for Valley Mental Health Foundation, Inc. and Valley Services, Inc. VMH exercises a certain amount of control over these entities, but VMH does not control a majority voting interest in the boards of directors of these entities.

	Valley Mental Health Foundation, Inc.	Valley Services, Inc.
December 31, 2006		
Total assets	$ 7,585,000	$ 1,839,000
Total liabilities	3,027,000	740,000
Net assets	4,570,000	1,099,000
Revenues	1,332,000	4,282,000
Expenses	964,000	4,535,000
December 31, 2005		
Total assets	$ 7,149,000	$ 1,702,000
Total liabilities	2,947,000	350,000
Net assets	4,202,000	1,352,000
Revenues	2,297,000	3,933,000
Expenses	858,000	4,012,000

VALLEY MENTAL HEALTH, INCORPORATED
Schedule of Expenditures of Federal Awards

Year Ended December 31, 2006

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantors' Numbers	Federal Expenditures
U.S. Department of Health and Human Services:			
Block Grant for Prevention and Treatment of Substance Abuse passed through Summit County	93.959	06-0008	326,270
Block Grant for Prevention and Treatment of Substance Abuse passed through Tooele County	93.959	05-2367	391,239
Total 93.959*			717,509
Block Grant for Community Mental Health Services passed through Salt Lake County	93.958	06-0305	906,900
Block Grant for Community Mental Health Services Passed through Summit County	93.958	06-0007	32,900
Block Grant for Community Mental Health Services Passed through Tooele County	93.958	05-2464	44,800
Total 93.958*			984,600

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantors' Numbers	Federal Expenditures
Refugee and Entrant Assistance passed through Utah Department of Human Services	93.566	00-2007	23,769
PATH Homeless Grant passed through Utah State Department of Human Services, Division of Mental Health and Salt Lake County	93.150	Z5-1301	244,489
Total U.S. Department of Health and Human Services			1,970,367
U.S. Department of Education:			
Drug Free Schools passed through Summit County	84.186B	06-0008	12,396
Drug Free Schools passed through Tooele County	84.186B	05-2367	13,754
Total U.S. Department of Education			26,150

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantors' Numbers	Federal Expenditures
U.S. Department of Agriculture:			
National School Lunch Program, School Breakfast Program, and Food Distribution Program, passed through Utah State Office of Education	10.550 10.553 10.555	A-1 C-8	175,107
Total U.S. Department of Agriculture			175,107
U.S. Department of Housing and Urban Development:			
Community Development Block Grant	14.218		7,000
Emergency Shelter Grant	14.231	BV05504	66,814
Supportive Housing Grant	14.235	00-2007	79,072
Total U.S. Department of Housing and Urban Development			152,886
Total Federal expenditures			$ 2,324,510

Note 1 – Basis of Presentation

The above schedule of expenditures of federal awards includes the federal grant activity of Valley Mental Health, Incorporated and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

* Denotes a major program

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THE CRITICAL KNOWLEDGE SOURCE
BUSINESS ADVISORS
AND CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Trustees of
Valley Mental Health, Incorporated

We have audited the consolidated financial statements of Valley Mental Health, Incorporated and Affiliates (the Organization) as of and for the year ended December 31, 2006, and have issued our report thereon dated April 30, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Valley Mental Health, Incorporated's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over consolidated financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies and material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Organization's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Organization's consolidated financial statements that is more than inconsequential will not be prevented or detected by the Organization's internal control. We consider the deficiency described in the accompanying schedule of findings and questioned costs numbered 2006-1 to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the consolidated financial statements will not be prevented or detected by the Organization's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs numbered 2006-2 and 2006-3 to be material weaknesses in internal control over financial reporting.

We also noted certain matters not considered significant deficiencies or material weaknesses that we reported to the management of the Organization in a separate letter dated April 30, 2007.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's consolidated financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The Organization's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Valley Mental Health's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information of the Board of Trustees, management, others within the Organization, federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by any one other than these specified parties.

Tanner LC

Salt Lake City, Utah
April 30, 2007

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THE CRITICAL KNOWLEDGE SOURCE
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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Trustees of
Valley Mental Health, Incorporated

Compliance

We have audited the compliance of Valley Mental Health, Incorporated (the Organization) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal programs for the year ended December 31, 2006. The Organization's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal programs are the responsibility of the Organization's management. Our responsibility is to express an opinion on the Organization's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Organization's compliance with those requirements.

In our opinion, Valley Mental Health, Incorporated complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended December 31, 2006.

Internal Control Over Compliance

The management of the Organization is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Organization's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over compliance.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the Organization's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material misstatement in relation to a major federal program will not be prevented or detected by the Organization's internal control. Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Board of Trustees, management, others within the Organization, Federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Tanner LC

Salt Lake City, Utah
April 30, 2007

Section 1 – Summary of Auditors' Results

Financial Statements

Type of auditors' report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified?	X yes	___ no
Significant deficiency(ies) identified that are not considered to be material weaknesses?	X yes	___ none reported
Noncompliance material to financial statements noted?	___ yes	X no

Federal Awards

Internal control over major programs:

Material weakness identified?	___ yes	X no
Significant deficiency(ies) identified that are not considered to be material weaknesses?	___ yes	X none reported

Type of auditor's report issued on compliance for major programs: Unqualified.

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?	X yes	___ no

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
93.959	Block Grant for Prevention and Treatment of Substance Abuse
93.958	Block Grant for Community Mental Health Services

Dollar threshold used to distinguish between type A and type B programs: $300,000

Auditee qualified as low-risk auditee?	___ yes	X no

Section II – Financial Statement Findings

2006-1 Timecard Approval

Criteria:
Employee and supervisory approval of electronic timecards is one of the Organization's internal control policies.

Condition:
During our audit we noted instances in which employees and supervisors had not approved electronic timecards.

Effect:
Without the proper approval of electronic timecards, inaccuracies in payroll amounts could potentially occur. One mitigating control in place is the comparison of monthly budgeted and actual expenses by unit managers.

Recommendation:
We recommend that management enforce policies and procedures to ensure that all electronic timecards are approved in the payroll system.

Management's Response:
Subsequent to year end, a management report has been created which, identifies all employee time that has not been approved by employees and or supervisors. Area Directors are then responsible to communicate VMH's policies regarding timely approval of electronic timecards to those identified on the report and to ensure proper approval. This report will be generated on a monthly basis and reviewed by the Executive Committee.

2006-2 Wire Transfers and Journal Entries

Criteria:
Segregation of incompatible duties is a key component of any system of internal control. The basic premise is that no one employee should have access to both physical assets and the related accounting records.

Condition:
We noted that the Comptroller can (1) create and release wire transfers and (2) create general ledger journal entries.

Effect:
When this situation exists, the individual has control of all phases of a transaction and therefore, the likelihood of misappropriation of assets is heightened.

Recommendation:
Although verbal approval is required prior to initiating a wire transfer and daily cash reconciliation is performed, we recommend that management, in cooperation with the Organization's bank, explore control options that eliminate the possibility of one person independently completing an electronic funds transfer.

Management's Response:
We have contacted and are working with our financial institution to explore possibilities of strengthening our controls over wire-transfers through options they have.

2006-3 Current Accounting Pronouncements

Criteria:
New accounting standards are periodically issued by various accounting standard-setting bodies. Certain of these new pronouncements have an effect on the presentation and disclosure of the Organization's consolidated financial statements. Certain new accounting guidance is issued in the form of interpretations and task force communications. Although this type of guidance is not as high profile as certain other accounting standards, the financial statement impact can be just as significant.

Condition:
One such standard is Emerging Issues Task Force Issue 04-5 *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights.* This guidance had not been identified for implementation by the Organization.

Effect:
This resulted in audit adjustments and consolidation of five tax credit housing projects into the Organization's consolidated financial statements for the year ended December 31, 2006.

Recommendation:
We recommend that management establish procedures to ensure that all new accounting pronouncements that may require changes to the Organization's accounting policies are identified and implemented. The burden of this task can be reduced through the use of an accounting standards update and library service.

Management's Response:
We are currently in the process of evaluating different on-line subscription services and plan to subscribe to a system that provides accounting pronouncement up-dates on a regular basis. New accounting standards will be evaluated to determine if adoption is required by VMH.

Section III – Federal Award Findings and Questioned Costs

No findings or questioned costs were noted related to our audit of the major federal award programs.

VALLEY MENTAL HEALTH, INCORPORATED
Summary Schedule of Prior Audit Findings

Year Ended December 31, 2006

The schedule of findings and questioned costs for the December 31, 2005 audit included no findings.